

**REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA
LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS
AND PERFORMANCE INFORMATION OF THE MBOMBELA LOCAL
MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Mbombela Local Municipality which comprise the statement of financial position as at 30 June 2009, and the statement of financial performance, the statement of changes in net assets and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages XX to XX.

The accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the Statements of Generally Recognised Accounting Practice (Statements of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Mbombela Local

Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.

7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for qualified opinion

Immovable property, plant and equipment

8. Sufficient appropriate audit evidence could not be obtained as to the existence, rights, completeness and valuation of immovable assets as disclosed in note 6 to the financial statements, to the carrying value of R1 853 543 631 for the current financial year and R1 214 503 606 for the previous financial year, due to the incomplete classification of assets in the fixed asset register. I was unable to perform suitable alternative procedures due to the poor quality of the fixed asset register, including a lack of descriptions, locations, asset numbers and/or bar codes.

Movable property, plant and equipment

9. The amount of R69 329 701 disclosed in note 6 to the financial statements as other assets differed from the fixed asset register amounting to R59 448 000, resulting in an overstatement of R9 881 701 in the financial statements.
10. Additions of movable assets as disclosed in note 6 to the financial statements were understated by R14 255 589, due to additions included at incorrect amounts in the fixed asset register. Therefore, the depreciation of these assets was also understated by an unknown amount. It was impracticable to quantify the misstatement, as the municipality's accounting records did not permit me to perform alternative procedures.
11. In terms of paragraph 84 of GRAP 17 *Property, Plant and Equipment*, an entity shall disclose the methods adopted and the estimated useful lives or depreciation rates to provide users of financial statements with information that allows them to review the policies selected by management and enables comparisons to be made with other entities. The depreciation charged for the current year on other assets as disclosed in note 6 to the financial statements was R2 127 966 and the amount calculated in the fixed asset register was R10 907 920. Therefore, the depreciation charge in the statement of financial performance and the accumulated depreciation in the statement of financial position were understated and the accumulated surplus was overstated by the difference of R8 779 954.
12. As disclosed in note 25 to the financial statements, a correction of error to the amount of R19 086 370 was made to fixed assets after a physical verification of movable assets had been performed. Due to the lack of supporting documentation, the accuracy of the correction could not be confirmed and sufficient appropriate evidence could therefore not be obtained as to the accuracy, completeness and existence of other assets to the amount of R19 086 370, as the amount was not assigned to any identifiable assets and supporting schedules could not be provided in respect of this adjustment. I was unable to perform suitable alternative procedures.
13. My opinion on property, plant and equipment was modified for the period ended 30 June 2008, due to a lack of supporting documentation. My opinion on the current period financial statements is also modified because of the possible effect of this matter on the comparability of the current period figures and the corresponding figures for property, plant and equipment, disclosed in note 6 to the financial statements.

Intangible assets

14. Assets classified as intangible assets, as disclosed in note 7 to the financial statements, did not meet the identifiability criteria of intangible assets as per GRAP 102 *Intangible Assets*. Consequently, a combination of other accounts were understated by R3 164 829 and intangible assets overstated by the said amount.

Revenue

15. Distribution losses of electricity for the 2008-09 financial year were not determined. As a result, I could not obtain sufficient appropriate audit evidence as to the completeness and accuracy of the accounting records, beyond the actual receipts recorded, and therefore revenue from the sale of electricity to the amount of R227 314 368 as disclosed in note 15 to the financial statements. The municipality's financial system did not permit me to perform alternative procedures.

Landfill provision

16. In terms of paragraph 25 of GRAP 17 *Property, Plant and Equipment*, the cost of an item of property, plant and equipment includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. A provision for landfill sites was not maintained by the municipality during the year under review as required. It was impracticable to quantify the effect of the misstatement, as no reporting information was available to determine the amount.

Qualified opinion

17. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Mbombela Local Municipality as at 30 June 2009 and its financial performance and its cash flows for the year then ended, in accordance with the Statements of GRAP and in the manner required by the MFMA.

Emphasis of matter

I draw attention to the following matter on which I do not express a qualified opinion:

Significant uncertainty

18. As disclosed in note 32 to the financial statements, the municipality is the defendant in a law-suit regarding the transfer of the land on which the FIFA 2010 World Cup Stadium is built. The municipality is opposing the interdict. The ultimate outcome of the matter cannot presently be determined, and no provision for any liability that may result has been made in the financial statements.

Restatement of corresponding figures

19. As disclosed in note 25.2 to the financial statements, the corresponding figures for 30 June 2008 have been restated as a result of errors discovered during the 2008-09 financial year in the financial statements of the municipality at, and for the year ended, 30 June 2008.

Other matters

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Unaudited supplementary schedules

20. The municipality provided supplementary information in the financial statements on whether resources were obtained and used in accordance with the legally adopted budget, in accordance with GRAP 1 *Presentation of Financial Statements*. The supplementary budget information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. Accordingly I do not express an opinion thereon.

Governance framework

21. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

Internal control deficiencies

22. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Par. no.	Basis for qualified opinion	CE	RA	CA	IC	M
8	Immovable property, plant and equipment	5	2	3	3	1
9 -13	Movable property, plant and equipment	5	2	3	1	1
14	Intangible assets	5	2	3	3	1
15	Departmental revenue	5	2	3	3	1
16	Landfill provision	5	2	3	3	1

23. Due to personnel acting in key senior management positions and capacity constraints in the finance department, effective leadership, supervision and monitoring was not exercised over financial reporting and internal control.

Legend	
CE = Control environment	
The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1
Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.	4

Legend	
The accounting officer/accounting authority does not exercise oversight responsibility over financial reporting and internal control.	5
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7
RA = Risk assessment	
Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5
CA = Control activities	
There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and communicated.	6
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7
IC = Information and communication	
Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3
M = Monitoring	
Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self-assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

Key governance responsibilities

24. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
Clear trail of supporting documentation that is easily available and provided in a timely manner			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.	Y	
Quality of financial statements and related management information			
2.	The financial statements were not subject to any material amendments resulting from the audit.		N
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.	Y	
Timeliness of financial statements and management information			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines (section 126 of the MFMA).	Y	
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.	Y	

No.	Matter	Y	N
Development of and compliance with risk management, effective internal control and governance practices			
6.	Audit committee		
	The municipality had an audit committee in operation throughout the financial year.	Y	
	The audit committee operates in accordance with approved, written terms of reference.	Y	
	The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.	Y	
7.	Internal audit		
	The municipality had an internal audit function in operation throughout the financial year.	Y	
	The internal audit function operates in terms of an approved internal audit plan.	Y	
	The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.	Y	
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		N
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.	Y	
10.	The information systems were appropriate to facilitate the preparation of the financial statements.	Y	
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.	Y	
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	Y	
Follow-up of audit findings			
13.	The prior year audit findings have been substantially addressed.	Y	
14.	SCOPA resolutions have been substantially implemented.	Y	
Issues relating to the reporting of performance information			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.	Y	
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		N
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the municipality against its mandate, predetermined objectives, outputs, indicators and targets in terms of section 68 of the MFMA.	Y	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.	Y	

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

25. I have reviewed the performance information as set out on pages XX to XX.

The accounting officer's responsibility for the performance information

26. In terms of section 121(3)(c) of the MFMA, the annual report of the municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

The Auditor-General's responsibility

27. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
28. In terms of the foregoing my engagement included performing procedures of an audit review nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
29. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the findings reported below.

Findings on performance information

Non-compliance with regulatory requirements

Content of integrated development plan

30. The integrated development plan of the municipality did not include key performance indicators and performance targets in terms of its performance management system, as required by sections 26(i) and 41(1)(b) of the MSA and regulation 12 of the Municipal Planning and Performance Management Regulations, 2001.

Existence and functioning of a performance audit committee

31. The performance audit committee did not review the fourth quarterly internal audit report of the performance measurements of the municipality.

APPRECIATION

32. The assistance rendered by the staff of the Mbombela Local Municipality during the audit is sincerely appreciated.

Auditor - General

Nelspruit

30 November 2009



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence